FOCUS ON RETIREMENT PLANNING

Make up for lost time with cash balance retirement plan

By MICHAEL JOYCE
Special for Lehigh Valley Business

When designing a retirement plan for employees, business owners have many options. From 401k plans to simple individual retirement accounts, each plan has specific advantages and disadvantages.


Joyce

One plan that is growing in influence among older business-owners is the cash balance plan. What sets it apart for business owners is that it has higher contribution limits that increase with age.

Older business-owners often need to make up for lost time on the retirement savings front after spending their prime savings years focused on building and investing in burgeoning companies. For them, the higher contribution limits permitted in cash balance plans are appealing, allowing them to accelerate retirement saving.

In 2017, the contribution limit for 401k plans with profit sharing is $59,000. With cash balance plans, business owners and executives are able to amass more pre-tax dollars – up to $137,000 in total employer and employee contributions for a 50-year-old, up to $235,000 for a 60-year-old and up to $303,000 for a 70-year-old.

Of course, significant cash flow is required for businesses to be able to make such sizable contributions to these plans.

EMPLOYER BEARS RISK

Participants in cash balance plans receive an annual pay credit (a percentage of compensation or a flat dollar amount), as well as an interest credit (at a fixed or variable rate linked to an index) from their employer.

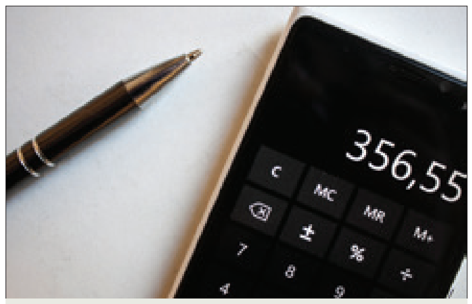
The plan's investments are professionally managed, and the employer bears the risk of the investments.

Since the rate of return is guaranteed and not dependent upon performance, the ups and downs of a plan's investments do not directly affect the benefit amounts received by participants.

LUMP SUM OPTION

According to the Department of Labor, cash balance plans are defined benefits plans that report like a defined contribution plan, with a "stated account balance."

At retirement age, participants are able to make a choice about how they receive their retirement earnings: Distributions can be taken as an annuity or as a lump sum benefit which can be rolled over into an IRA or another employer's plan.



KEY TAKEAWAYS

Business owners would be wise to weigh the pros and cons of establishing a cash balance plan for employees. While there are drawbacks to consider, cash balance plans:

- Offer a guaranteed retirement benefit to a team of employees.
- Simultaneously facilitate greater tax-deferred retirement savings for executives and partners.

The common practice – and the recommended one – is to take the distribution as a lump sum benefit.

CUSTOMIZED CONTRIBUTIONS

An advantage of cash balance plans is that they can be customized to reward varying employee levels within an organization, from owner to partner to staff. Different dollar amounts can be credited to each level of employee (as a percentage of pay or a flat dollar amount).

Also, the plans are Internal Revenue Service-qualified, tax-deferred, secure under the Employee Retirement Income Security Act and protected from creditors.

A potential downside of these plans is that they are invested more conservatively than other investment vehicles, resulting in modest (but often steady) returns.

As with traditional defined benefits pension plans, the business owner and plan manager strive to match assets (plan balances) and liabilities (future payouts).

ADMINISTRATIVE EXPENSES

Additionally, employers are required to make contributions to employees' plans each year, so businesses offering this benefit must have stability of profits and cash flow.

Also, the actuarial and administrative expenses required for plan oversight are more costly than other plan types.

Administrative fees usually range from $2,000-$10,000 annually, and investment management fees can be 0.25 percent to 1 percent of assets.

GUARANTEED ANNUITY

From the employee perspective, shifting

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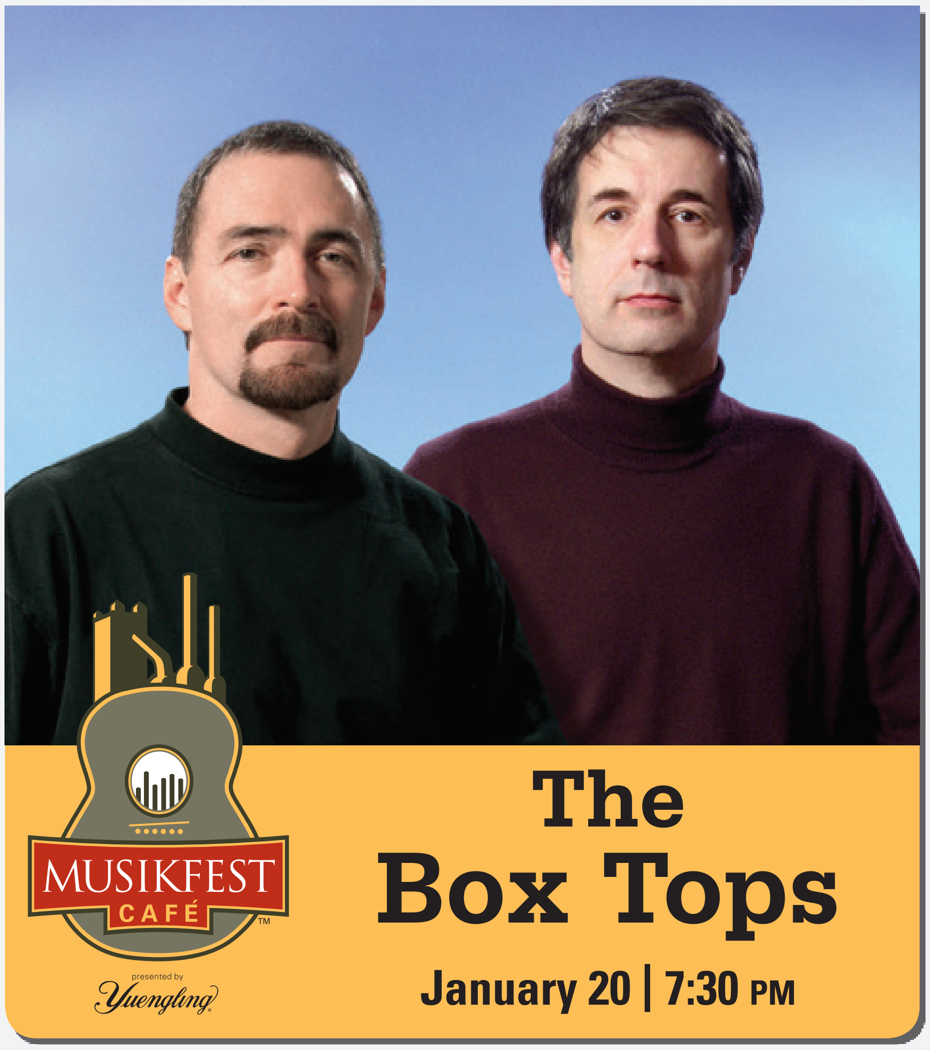

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BANKS

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efit how banks operate and contribute to the economy. Even the end of the election cycle itself has spurred confidence in the economy.

"I think all of our members would like to see some level of regulatory relief with this administration," said Duncan Campbell, president and CEO of the Pennsylvania Bankers Association, a trade organization in Harrisburg. "We are cautiously hopeful. Again, we don't know what to expect."

With a slimming of federally imposed regulations, bankers say, they can focus on investing more money in the communities they serve.

"They are the local economic engines; they want to be out in the community and lending," Campbell said.

Bankers say regulations, though necessary to some degree for protecting consumers, are hindering their ability to grow.


Koppmann

While some regulations are essential for the industry to function and thrive, the amount of regulations could be lessened, many bank executives say.

"It's caused us to make some heightened changes in our compliance infrastructure risk management," said Tom Koppmann, regional president of M&T Bank's eastern Pennsylvania region.

MONEY BETTER SPENT ELSEWHERE

The comprehensive law requires many banks to increase their staff or spend more time making sure they understand and are following the regulations, time, they say, that could be better spent.

When Dodd-Frank came out in 2010, it was composed of more than 20,000 pages of compliance rules for the banking industry, a significant amount of regulation being brought to an industry with limited resources, Campbell said.

While it could be argued that the banking industry needed additional oversight after the economic recession of 2008, the challenges banks now face involve excessive regulations, said Gerry Nau, chairman and CEO of Lafayette Ambassador Bank in Bethlehem.

> 'The problem with Dodd-Frank is it's touched every aspect of a bank and paints them all with the same brush.'
>
> — Gerry Nau, Lafayette Ambassador Bank

ONE SIZE FITS ALL

Nau said some good things came out of the Dodd-Frank Act, including giving banks the power to address systematic threats so they can stress-test their business models to see how they would operate in a severe financial crisis.

"The problem with Dodd-Frank is it's touched every aspect of a bank and paints them all with the same brush," Nau said. "Instead of investing a lot of that money into the community, that investment [by banks] became internal. It's not a formula you want to see continuing."

As an example, under Dodd-Frank, the consumer does not always realize that the amount of paperwork for a mortgage is needed because the regulators require it, Campbell said.

CUSTOMIZED RULES

Having tailored bank regulations is one theme Nau said most bankers could agree on, so that conservative community and regional banks are not regulated the same as banks that have a high-risk profile.

"It would be great to see a bank or law that would recognize banks differently based on how they run their business," Nau said.

Campbell also said he supported the need for banks to have tailored regulations rather than a one-size-fits-all approach.

MORTGAGE RELIEF

Another aspect of Dodd-Frank that Nau would like to see reduced are mortgage rules. While Nau said it's an admirable goal to avoid the subprime mortgage lending crisis that other banks engaged in, there are fewer first-time homebuyers and the mortgage business has become a product for those with high credit scores.

During the subprime mortgage crisis, many banks offered loans to homeowners who had low credit scores. Nearly 10 years after the economic crisis, Nau said, bankers are hoping for mortgage relief.

While a complete overhaul of Dodd-Frank is unlikely, there are pieces of the law that could be reduced to alleviate some of the challenges in that law, Nau said.

"I think the entire industry could use relief," he said. "The industry as a whole supports economic activity."

MORE ABILITY TO LEND

If banking regulations are lessened, that could make it easier for banks to loan money.

As a result, commercial construction loans are expected to increase in 2017 for banks, judging by the strong amount of interest in new industrial properties.

Overall, the Greater Lehigh Valley's economy appears to be moving in the right direction, and Nau said he is optimistic.

"Banks generally feed off that growth but support it, as well," Nau said. "We are seeing growth in virtually every major sector."

CONFIDENCE REIGNS

For the past year, loan demand has been very good for banks doing business in the region, said Bill Long, administrative vice president of corporate banking for M&T's Lehigh and Berks County region.

Development along the Route 33 and Interstate 78 corridors continues without end, and more development is expected in Berks County's industrial parks, Long said.

"In Berks, some of the companies that are already established here continue to do well," Long said. "If you look at the economy, consumer spending is doing well. I think people were holding back because of election results. I think people are relieved it's over. The businesspeople I talked to are pretty confident."

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> — Bill Long, M&T Bank

If businesses are more confident in the economy, that will help boost the lending environment for construction and also improve auto and retail sales, Koppmann said.

CITY HALL

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developer to have a development package ready to submit for the largest allocation of new market tax credits ever dispersed by the U.S. Treasury department, the primary focus of which is to catalyze private development in mostly distressed urban areas.

Numerous agencies that received the tax credits were all but begging to do projects in downtown Reading, but City Hall did not/would not work with any private developers to have projects ready for funding.

SMALL BUSINESSES SUFFER

Once again we are witnessing a City Hall administration unwilling to show the leadership and spirit of cooperation that it was elected and hired to provide.

In the end, it is the small businesses and citizens that are the backbone of our community that continue to suffer the consequences.

The potentially good news: We can always hope for a better 2017.

Alan Shuman is owner and broker of record of Shuman Development Group, which has redeveloped the buildings at the former Reading Outlet Center in the city. He can be reached at 610-736-3033 or sdg@investinreading.com.

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to a cash balance plan from a traditional pension plan can result in diminished benefits.

Traditional pension plan payouts are usually linked to an employee's highest annual earnings, whereas cash balance plan payouts are linked to earnings across the working history – from lowest earnings to highest.

But having the option of a guaranteed annuity that these plans provide can be attractive to workers.

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